AGENDA

SPECIAL COMMITTEE ON ESTABLISHING A MANCHESTER PUBLIC BANK

May 03, 2016	**5:30 p.m.**
Aldermen Herbert, Ludwig,	**Aldermanic Chambers**
O'Neil, Barry, Cavanaugh	**City Hall (3rd Floor)**

1. Chairman Herbert calls the meeting to order.

2. The Clerk calls the roll.

3. Discussion regarding the City's Comprehensive Annual Financial Report (CAFR).

4. Discussion regarding the formation of a municipal bank.
   Gentlemen, what is your pleasure?

5. If there is no further business, a motion is in order to adjourn.

Public Banks for U.S. Cities

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The Public Bank Project is dedicated to developing financial alternatives to the current system of Wall Street dominated finance to expand the policy options and autonomy of local governments. Our particular focus is on how local governments can pursue innovative policy initiatives to increase public sector investments in areas such as affordable housing, infrastructure, and targeted economic development within low-income neighborhoods and communities. We are dedicated to reinvigorating the relation between citizens and local government, and to promoting projects that create more socially just and ecologically sound cities.

I. Introduction

Since the financial crisis of 2008-2009, and the government bail-out of the "too big to fail" Wall Street banks, there has been growing dissatisfaction across the U.S. with the domination of our financial system by large corporate banks, and growing interest in the idea of public banking.

Over the last two years, the Public Bank Project, in partnership with San Francisco Supervisor John Avalos's office, has developed a basic template for the establishment, funding, and operation of a municipal bank applicable to any of the one hundred and twenty-one charter cities in California. Subject to modifications specific to laws in other states, this basic template provides a model that could be instituted in other U.S. states that grant substantial "home rule powers" to local governments.

What follows is a brief overview of how a municipal bank could be constituted, and the types of activities toward which its financial capacities could be directed.

II. The Need for alternatives

Despite widespread sentiment that the current U.S. financial system serves the interests of a rich and powerful minority, there is a widely-held perception that there are few, in any, meaningful financing alternatives available to local governments that could be implemented within the current legal, regulatory, and political context. The unfortunate result is that progressive initiatives to support affordable housing development, to defend existing residents from displacement due to market-led redevelopment, and to undertake longer-term infrastructure investments are repeatedly sacrificed to the grim realities of lack of financial resources necessary to fund such initiatives. Popular campaigns accordingly focus largely on achieving better and more transparent regulation of private financial interests, such as more transparent disclosure of loans terms and better consumer protections against financial fraud. While better oversight of powerful financial actors is certainly a highly laudable goal in and of itself, it fails to offer any solutions to the present fiscal limits that constrict the ability of local governments and urban residents to pursue more inclusive and socially equitable programs of local development. Clearly, there is a need to develop more far-reaching alternatives to current U.S. financial arrangements in order to expand the policy options available to local governments.

III. Developing real solutions

Municipal banks are a potentially powerful, and highly innovative, policy option available to cities in states with strong "home rule" provisions in their state constitution and statutes. They provide a means to tap often-significant local and regional financial resources currently held as deposits with private banking establishments. In addition, surpluses invested in various short-term money market instruments could be recaptured and directed back into supporting increased local investments in affordable housing, infrastructure, and community-based economic development.

Municipal banks will not, by themselves, solve the full spectrum of fiscal and economic challenges facing U.S. cities and working-class residents. However, if combined with well-crafted local tax policies, and the powers vested in many U.S. municipalities over land use and setting conditions on private developers, they offer a powerful means to significantly expand the policy options available to local governments. They can do so, moreover, in ways that reverses decades of devaluation of the public sector by reaffirming the positive, even transformative, role of government as an agent of social improvement.1

IV. A proposal for transforming the current system of municipal finance
What follows is a brief overview of the way local governments can use home rule powers to create and operate locally controlled systems of democratically accountable public finance.2 It is predicated upon the belief that local governments can, and must, create new tools to pursue policies of socially just and equitable development. Cities can establish locally controlled, municipal public banks, and use the financial resources to fund critical needs such as affordable housing, economic development in low-income neighborhoods, and more energy-efficient (CO_2-reducing) forms of infrastructure development.

Municipal banks could also become powerful partners to existing community banks, credit unions, and community-development financial institutions, enabling them to extend their services to households that are currently underserved – or even exploited – by present U.S. financial arrangements. Moreover, they can do so in ways that insure enhanced accountability of municipal governments to local residents, and that provide a real-world model for reinvigorating the relationship between citizens and local government.

V. Options for implementation

Local governments have two broad options available for establishing locally owned and controlled municipal financial institutions. Option 1 is to create a full-fledged, state-chartered depository institution outright, through either a Council ordinance or a voter-approved Charter Amendment. Option 2 is to embark on a two-stage process that would first establish a non-depository Municipal Development Corporation that could begin to make long-term housing and infrastructure investments, together with a smaller-scaled, limited-purpose depository institution. Once this entity is in operation, the municipality could then expand its operations to establish a locally controlled depository institution that would take over all depository and cash management services currently contracted by the city with private commercial banking institutions.

Option 1: Creating the municipal banking institution
A city would establish a public bank through either an ordinance or a Charter Amendment. The bank would be a legally separate entity from the city, incorporated under state charter as an independent banking institution. Different legal forms of incorporation exist in various states; in California, a public bank could be incorporated as a Legal Benefit Corporation. This is a form of incorporation in which explicit provisions pertaining to broad public policy goals are set out in the Articles of Incorporation. In order to ensure operational autonomy from City politics, an independent Board of Directors would govern the Bank. Members would be appointed by the Mayor and City Council (or Board of Supervisors if constituted at the county level), but would thereafter have full autonomy in overseeing management and insuring that the Bank continued to fulfill the founding policy goals set forth in the founding Articles. Board members would be selected according to criteria such as requisite expertise, demonstrated commitment to the mission of the Bank, and representation of constituencies typically excluded from decisions about public finance.

Shares in the Bank (Bank stock) would be organized into various classes structured to insure that the municipal government, as the ultimate controlling corporate entity, remains the sole controlling interest through exclusive power to appoint the Board of Directors. Retaining exclusive power of appointment is essential to insuring continued fulfillment of the public purpose and objectives that motivated the establishment of the Bank. The municipality, as the ultimate controlling interest, could either own the Bank in its entirety or sell non-controlling classes of shares to other investors. Owners of these subordinated share classes would be eligible to receive dividend payments, but would not exercise any controlling influence on Bank policy or the selection of the Board. The City would at all times retain ultimate authority and oversight; any subsequent amendment or dilution of control could occur only through an ordinance whose ratification would be subject to legislative approval by the City Council.

A public bank would funded through a variety of sources and vehicles, including: 1) the City's own equity investment, funded through a one-time appropriation from the General Fund or transfers of assets from the municipality's existing investment pool; 2) equity investments in non-voting shares sold to other local governments and pension funds; 3) transfer of the City's deposits and cash accounts currently held in large commercial banking institutions; 4) the issue of debt (short-term and medium-term notes) purchased using funds under management by the City Treasurer; 5) the issue of Certificates of Deposit sold to the Treasurer and other "outside" investors; 6) banker's acceptances; and 7) repo-like operations that would be conducted with the City Treasurer to insure adequate provision of short-term liquidity. Additional funding sources could include equity investments by "outside" investors (other local governments, pension funds); bank deposits from local governments, pension funds, public-sector unions, and socially oriented nonprofits; and, where financially prudent, the issuance of additional medium-term debt (medium-term notes). The Bank could also issue bonds of longer duration to finance long-term investments in affordable housing and infrastructure development.

The Bank would use this funding base to support affordable housing and large-scale infrastructure development. In addition, the Bank could support economic development in low-income neighborhoods in partnership with local banks and credit unions that have established branches, relationships, and retail lending outlets. To maintain low overhead costs (and to avoid competition with local lenders), the Bank would not operate an extensive network of retail branches. Loans provided to local residents and businesses would be evaluated by the Bank's partners, with the Municipal Bank serving primarily to provide additional funding through participation loans. All lending activity would be subject to rigorous evaluation to insure that credit allocation is fully independent of political considerations and fulfills the public policy goals set out in the Bank's founding Policy Statement.

Option 2: A two-stage process for creating a new system of equitable and just local finance
In option 2, the provisions outlined above regarding ownership, the structuring of various classes of shares, and the independence and composition of the Board are largely identical. The difference is that the establishment of a locally controlled financial institution would occur through a two-stage process of formation. The first stage involves creating a non-depository Municipal Development Corporation that will issue medium-term notes to raise funds for investing in capital projects and affordable housing. The funds raised by affordable housing developers would be placed in a complementary depository entity – the Municipal Bank – that would begin to carry out basic account management and payment services on behalf of these nonprofit entities. The depository bank could similarly begin to accept deposits from nonprofit organizations, unions, and pension funds to expand its operational capacities.

The second stage is the application to the Federal Home Loan Bank for a letter of credit that will satisfy state-level requirements for the full collateralization of public-sector deposits. This will allow the bank to conduct all depository and cash-management services, overdraft services, sweep arrangements, and provision of short-term lines of credit to local governments. Both the Municipal Development Corporation and the Municipal Bank will be incorporated and chartered as entities legally separate from the City. These entities will entail no ongoing need for General Fund revenue, nor will the formation of these entities necessitate higher taxes. The municipal legal entity that is set up to hold and vote the city's controlling interest – the Municipal Financial Corporation would be defined as a Bank Holding Company per USC 12, Sec. 1841, and hence would be subject to oversight by the Federal Reserve. The municipality will at all times retain sole controlling interest, vested with exclusive rights over Board appointments, and would vote the municipality's stock as the sole directing interest. The City retains the right to dissolve and reconstitute the Board should the Board fail to insure that the Municipal Financial Corporation is acting to fulfill its founding public purpose.

VI. Hardwiring a democratic, equitable public purpose and public mandate

Charter or home-rule cities have three broad pathways by which to pursue the formation of a public bank. Specifics of these options will vary by state; what follows are broad guidelines for thinking about actual implementation strategies for creating a municipal bank.

The first is through a one-time line-item appropriation proposed by the Mayor and ratified by the City Council (or Board of Supervisors if the bank is created at the county level). This would provide the initial equity investment required to move toward the establishment and organization of the Municipal Financial Corporation, and later a full-fledged Municipal Bank. That appropriation would be matched by a directive, initiated either through executive action or by the order of the legislative body, compelling the relevant county and city departments to undertake the necessary steps to establish and incorporate a legally independent, state-chartered banking corporation.

Second, the Corporation (and Bank) can be established through a legislative ordinance that would directly modify the City Charter to include provisions for establishing the Bank, with a full and explicit outline of founding purposes and the compelling public policy objectives to be served by the institution.

Third, the Corporation or Bank can be created through a citywide voter-approved Charter Amendment.

We believe that, where possible, the Charter Amendment is the preferable choice. It can guarantee that the Municipal Financial Corporation, and later the Municipal Bank, are constituted to fulfill a public purpose (e.g., to provide funding for investments not supported by the private market). A Charter Amendment also insures democratic ratification of the founding mandate by the voting public, which will significantly enhance the legitimacy of the Bank amongst the voting public.

In addition, a Charter Amendment is the strongest means to "hardwire" economic and social equity goals into the operation and governance of the Bank, and to insure that the Bank's founding policy goals and objectives will not be subverted – for instance, by directing funds toward high-end, market-rate housing development.

Funding the bank would require a financial commitment from the city's General Fund and/or its investment pool. In cities facing budget crises, this creates a potential barrier that must be addressed. We believe that innovative means exist to create funding pools for the Bank's capitalization and investment activities. The most important requirements will be to develop the political will, build local coalitions, and insure the buy-in of key local government agencies and officials.

VII. Risk management

Given the technical complexities of risk management, those interested in this aspect of the structure and operations of the Municipal Financial Corporation should consult the longer document available at municipalfinance.us.

Appendix A

Below is a simplified mock-up balance sheet of the Municipal Bank. We have included separate accounts of the non-depository and depository entities (if incorporated separately) or divisions (if part of a single entity). Creating a non-depository institution prior to the establishment of a full-spectrum institutional depository institution has advantages, given that non-depository entities have far less onerous capitalization and regulatory requirements.

<u>Municipal Development Corporation (non-depository)</u>

Assets	**Liabilities**
$450m loans and investments)	$450m (medium-term notes)

<u>Municipal Bank (depository)</u>

Assets	**Liabilities**
$200m (3-month Treasuries)	$100m (City and other equity)
$350m (loans and investments)	$100m (CDs)
	$250 (City deposits)
	$100m (other deposits)

<u>Municipal Financial Corporation (Bank Holding Company) aggregated balance sheet</u>

Assets	**Liabilities**
$200m (3-month Treasuries)	$100m (City and other equity)
$800m (loans and investments)	$250m (deposits)
	$100m (CDs)
	$450m (medium-term notes)

The depository institution would serve as the banking agent for the non-depository entity. Over time, the Bank would attract funding from additional sources, including other local governments and public agencies, pension funds, and social investors. Capitalization of earnings would be a source of additional growth.